Elaboration of the Principles of the European Union's Industrial Policy for Conditions of the Slovak Republic

(Strategy for Slovak industry development for the 21st century)

I. INTRODUCTION

In the economically advanced countries, there is a wide variety of approaches to industrial policy. Differences in approach depend on different levels of economic development, traditions and different institutional conditions such as centralisation or decentralised forms of administration.

The traditional form of industrial policy was characterised by direct government interventions through state-owned enterprises, direct subsidies in certain branches (often just in traditional and declining branches like metallurgy, shipbuilding, but also newer branches like electronics and aircraft production) by protecting such branches including the protection against imports.

Governments of respective states – including the Slovak Cabinet – can less and less afford to apply such an industrial policy, namely for a number of reasons. First of all it is the fact that government interventions have not always been the best and most effective support for economic development and the governments have been criticized for being unable to "recognize the winners."

Slovakia´s own experiences and knowledge as well as other countries´ experiences and knowledge are proving that market forces are a more reliable tool for developing a country´s production potential. This is also suggested by the fact that the management of privately-owned companies has to function in tougher conditions and is forced to attain a higher quality than that in the public sector, and a clear-cut profit-making orientation results in an improved effectiveness for privately-owned companies. This is the fundamental reason for global trend under which governments started privatising state-run companies in those countries where a bulk of industries was held by the state. A need to give a check to growth in public debt was a factor widely instrumental in supporting the privatisation process particularly in European countries – and this fact is true of the Slovak Republic too. Yet another significant factor was the occurrence of deficits of trade balances and a rise in total foreign debt of the countries.

A new phenomenon of states competition has gradually emerged in encouraging foreign investment inflows offered by the deepening world economy globalisation, while creating as attractive business environment for investment as possible. FDI inflows have been perceived by individual states as a major way of dynamizing the economic growth and thus raising the country´s population welfare.

Advanced states primarily for these indicated reasons came to understand that industrial policy, traditionally viewed quite narrowly and separately from the other policies targeted toward underpinning the economy structural adaptation, forms too narrow a framework to economically support structural-adaptation processes and growth in the country´s competitiveness. Therefore their understanding of economic-political support for these processes is leading toward what is now referred to in both theory and practice as competitiveness policy.

The basic framework for competitiveness policy in advanced states consists basically of three areas:

- strengthening and consolidation of macroeconomic stability and equilibrium,
- reforming and completion of the institutional environment having a significant impact on the conduct of companies,
- application of certain specific policies, indirectly conducive to growth in competitiveness through selected, especially horizontally cross-sectional areas of the economy.

These three areas are all the more of importance to the Slovak Republic that industry occupies, by way of its contributions to exports, GDP, employment and resource formation for the other branches, an irreplaceable place in the Slovak economy's economic results. Even the maintenance of economic stability of the whole economy depends on a successfully implemented competitiveness policy, by way of which the conditions will be created to improve competitiveness of individual branches of Slovak industry first of all on the European Union's single market and the markets of the countries included in the first round of negotiations on joining the EU.

Many even in this country understand by an industrial policy pinning down ”strategic enterprises” and ”strategic industries” whose development calls for the use of specific industrial policy instruments, which are most frequently subsidies, cheap loans, protection from competition and, last but not least, direct state ownership.

From the perspective of this approach, industrial policy is only acceptable when it contains objectives for matter-of-fact control of the economy. The industrial policy being presented is bound to disappoint these expectations. Its primary instruments are not direct interventions in the functioning of the market, which price setting, production volume control and planning development of both indicators into the future can be deemed to pose, but it is above all the removal of barriers preventing the market from functioning and the improvement of framework conditions for its functioning.

II. SLOVAK REPUBLIC´S INDUSTRIAL POLICY IN THE 1990´s: EXPERIENCE AND PROBLEMS

2.1. Environment destabilisation

Based on the results recorded in 1998 (see Annex 1), Slovakia's economic developments are characterised by a slowdown in economic growth and a further deepening of macroeconomic disproportions. Total gross debt increased, approaching the critical value of 60 % toward the end of 1998. A whopping adverse balance with a high of 80.8 billion Sk in 1998 persists in foreign trade. Similarly, the 1998 state budget ended up with a balance of –19.2 mld. Sk (2.7 % off GDP). High interest rates and a severe tax burden do not allow for development of serious business. Tensions are mounting in a host of companies that are not able to place their production on the domestic and foreign markets and default on their obligations, which risks massive shutdowns and climbing unemployment.

The above developments are the result of a combined effect of objective and subjective factors alike.

Among objective factors is an inadequate structure of the economy with a dominant position of heavy industry, which came into being over a historically relatively brief period of several decades and which had been influenced by ideological and geopolitical rather than primarily economical factors. The world's economy developments, and in particular developments of Slovakia's major trading partners, are also an important objective parameter for Slovak industry developments.

Subjective factors encompass first of all industrial policy mistakes that have led to a destabilisation of the business environment, including, but without limitation to:

- expansionary fiscal policy,
- nontransparent privatisation.

A direct consequence of the expansionary budgetary policy for industrial companies is a very high price for borrowing, which at first made financial expenses of companies to rise and thereafter led to a non-availability of domestic borrowing and search for financial resources abroad.

Slovakia's business sphere thus broke into two groups. The first, larger, has had no access to foreign borrowing and accordingly has exclusively relied on costly domestic borrowing. The second, smaller, which has had access to international financial markets (mostly owing to state guarantees granted) and which has handled the lack of domestic borrowing through credit expansion abroad inevitably accompanied by an increased exchange risk. Following floating the Slovak crown, the risk has been fully borne by companies, an overwhelming majority of which have failed to take advantage of the so-called exchange rate hedging.

Thus the expansionary budget policy from the previous period is responsible for a tremendous increase in financial expenses of the business sphere in the form of both high interests on domestic loans and realized exchange rate losses on foreign currency loans.

A direct consequence of the nontransparent privatisation and of the more or less openly declared preferential treatment of buyers from among domestic applicants, are nontransparent ownership relations. While new owners, often hiding behind puppets, acquired companies, they did not have capital needed to develop them. Taking no account of intentional tunneling of the companies and anticipating just best intentions of the new company owners, the main barrier to their possible restructuring and development has become the method of privatisation whose product is paradoxically new owners as well.

The economic policy on macroeconomic level was thus reflected in the microsphere through a huge increase in indebtedness of companies and their marked and long term undercapitalisation.

2.2. Isolationism

A so-called Slovak path of transformation has had a negative impact on Slovak industry. A part of it was the transformation of property relations by the indicated favouring domestic applicants in selling industrial companies owned by the state.

Favouring domestic buyers in the privatisation process implied at the same time discrimination against potential foreign investors. This fact manifested itself in a gradually profounding mistrust and growing prudence on the part of foreign partners.

As a result, the Slovak economy became isolated to a certain extent, showing the least participation in international capital flows compared with the region's other countries, especially the lowest foreign direct investment inflow.

Foreign direct investment inflows in CEFTA countries (mil. US$, in cumulative and per capita terms)

	Cumulative FDI						Per capita FDI
	1993	1994	1995	1996	1997	1998	1998
Slovakia	366	552	733	1,328	1,517	1,700	436
Czech R.	2,153	3,191	5,923	7,061	6,763	8,700	844
Poland	2,828	4,321	6,832	12,028	17,705	30,700	795
Hungary	6,632	8,316	13,265	16,093	17,529	19,400	1,902
Slovenia	954	1,331	1,754	1,934	2,400	2,600	1,300

Source: Foreign Direct Investment in Central and East European Countries, WIIW, Vienna July 1999

Foreign capital in Slovak industry

As of the end of 1998, foreign investment in Slovakia's industrial production (35.5 billion Sk) accounted for 48.5 % off total FDI.

The above data points out a remarkable deficit of foreign direct investment in Slovakia compared with the other V4 countries, in absolute or per capita terms.

On the other hand it should be noted that a high share of foreign direct investment was channeled in the neighbouring countries also to so-called natural monopolies which are owned by the state in Slovakia. Allowing for the purchase of just minority stakes in these companies would lead to a change in this indicator in favour of Slovakia, since capital inflows in the other countries have already occurred or are now occurring.

2.3. Conservation of the existing industrial structure

The low FDI inflow was also a contributing factor in a high degree in the insufficient change of Slovakia's industrial structure, since a substantial change in the industrial structure and growth dynamism owing to foreign direct investment can be seen in such examples as Hungary or Poland. The share of industry with a high degree of finalization and competitiveness in demanding markets is on the rise in these countries. This has been one of the basic objectives of Slovakia's industrial policy, but the achieved results do not prove it.

Restructuring of production, other activities and the overall orientation of a company are always a finance intensive process. The inadequate progress in restructuring Slovak industry, which resulted in some cases in a conservation of the existing, thus inconvenient, industrial structure, is a consequence to a large extent of the overall environment destabilisation.

From the company's perspective, there were four potential sources of funding restructuring:

1. own profit,
2. borrowing,
3. capital increase,
4. direct state subsidy.

An imbalance in the financial market invoked by the state caused a rise in interest rates and subsequent non-availability of borrowing as well as a decrease in profit due to increased financial expenses. The policy discouraging foreign investors prevented companies from access to capital as a potential source of funding restructuring.

The state budget resources did not become it either, so the overall effect of the short-termly expansionary policy was an acute lack of own or credit and capital resources for restructuring.

Under these conditions restructuring was impossible even provided that company owners and management would have been eminently interested in it.

2.4. Incapacity to deal with the problems of industry

Among the problems which a range of companies from a number of industries have to wrestle with are for example: producers low financial liquidity, financial provision for contracted production, technological obsoleteness, costly borrowing, the lack of own investment resources, the absence of strategic parners to restore technical and technological level of low quality level of the whole production process, inadequate company management level, etc.

An example of incapacity to handle the given problems, in particular insolvency problems, is Act on Revitalisation No. 211/1997 Coll. The Revitalisation Act was drafted all along in a non-functional manner and without resource provision. The used formulation that the revitalisation did not take place because of creditors´ refusal to agree with debtors is misleading and oversimplified. As goes industries under the province of the Slovak Economy Ministry, indeed there were only eight real and active companies interested in revitalisation and merely two companies sought to overcome the unbending bureacracy and the nonfeasible enforcement of the Revitalisation Act through to the end. There had not been created legal prerequisites to give effect to the forms of revitalisation, and in view of creditors´ discordant opinions not a single request had been finally discussed for industries.

Indeed, the given approach to dealing with the problems of Slovak industry solved nothing, yet on the contrary it contributed to deepening them by sending a very bad signal toward the corporate sphere in the shape of willingeness to support those who had been long termly demonstrating their inability to start functioning effectively.

2.5. Low effectiveness (counterproductivity) of funds spent

Within the foregoing efforts also a concept of bailing out the corporate sphere had been developed, with emphasis on the companies with a marked export potential, dominant defence production and engineering companies with special stress on restructuring the existing credit portfolio of the engineering companies which were to get involved in the implementation of selected programs of production. To this end, a sum of 2 billion Sk was earmarked from the 1997 state budget, which was however – today it can be said fortunately – never used for this purpose.

The problems of engineering firms and DMD, a.s., Holding were later on dealt with through bills of exchange accepted by SPP, š.p., Bratislava. While this non-concept averted for a time an open manifestation of the crisis in engineering companies first of all during the run-up to the election, it failed to resolve the situation. In this way some 2 billion Sk were siphoned off from SPP, š.p., resources, which are irrevocably lost, failing to bring about the expected start of mechanical engineering development.

The above non-concept at the same time makes it much more difficult to estimate the total volume of funds directed toward Slovak industry development or restructuring. In other words, it is very difficult to quantify costs related to the implementation of Slovak industrial policy.

One of possible ways of quantitifaction is the summary of expenditure in the form of direct subsidies, support for SME, industrial research, education/training and requalification expense as well as tax expense in the form of reliefs for domestic and foreign investors.

For individual types of support for the business environment (excluding agriculture), the following funds were drawn in 1996 and 1997:

Type of assistance Form of assistance Assistance amount in million Sk

	1996	**1997**
Research and development subsidies	546.0	509,0
SMEs lower interest rates	101.5	153,3
nonrep.contrib., realis.guarantees	87,5	132,2
Environmental management realised guarantees	81,7	102,0
Investment support realised state	1	1

	923,5	602,3
Regional aid subsidies	40,0	49,5
Export aid nonrepayable contributions	0	38,0
Aid from municipal budgets subsidies	59,4	143,9
Active employment policy nonrep. and repayable contr.	1 165,1	1 938,8
Taxation aid payment remission and lowering	6 358,1	1 598,2
State aid granted	10 566,4	5 464,5

Source: "A report on granted state aid in the Slovak Republic for 1997" approved by THE Slovak Government's Decree No. 583/99

III. A NEW STRATEGY FOR SLOVAK INDUSTRY DEVELOPMENT

3.1. Definition of a new vision

As suggested by the preceding analysis, the problems of Slovak industry are long-term and deeply rooted in both historical developments of the industrial structure and wrong industrial policy.

Half a million army of the jobless is proving that the state expansionary policy is not capable of dealing with the unemployment problem from the long-term perspective. It is high time to realize that a high price in the form of a severe tax burden financing the repayment of interests must be paid for credit funding of a short-termly high rate of economic growth.

It follows from today's economy status that following the 10 years of transformation Slovak industry and the whole economy face the need for a sweeping and deep-seated restructuring. Consequently, this fact warrants to note that the hitherto industrial policy has failed.

Both the hitherto overall economic policy and the hitherto industrial policy: 1. not only have not managed to create the conditions for a in the structure of Slovak industry, but in particular 2. have shown that a different approach is needed to improve the performance of industrial companies, as is an entirely new definition of the content, principles, objectives, instruments and the institutional framework of industrial policy.

Therefore it is high time to change the approach. It should be openly stated that there are short-term, fast and cheap solutions around to resolve the grave problems of Slovak industry and the economy as a whole. Similarly, there is not money available with which new and sustainable jobs could be immediately created.

Based on own experience from the past years, taking account of the errors and mistakes of industrial and economic policies in the previous periods, it is necessary to formulate an industrial policy setting itself the following objectives and residing in the following principles:

3.1.1. Industrial policy objectives

Industrial policy objectives must be ambitious on the one hand, yet realistic and attainable on the other hand.

Drawing on the needs of Slovak industry and the whole Slovak economy, industrial policy faces the task of adopting of measures, through the implementation of which the following is to be accomplished:

1. reduction in redundant capacities of Slovak industry in those areas which cannot compete on international markets and which long termly tie down substantial production capacities and labour, thereby conserving the existing – thus inconvenient – industrial structure. The release of such capacities – while considering the impacts of requisite restructuring upon unemployment and regions – that are currently concentrated in traditional industries, is a step necessary to shift economic activities toward more modern industries.
2. parallely shifting production factors (capital, labour, technologies) toward new areas, while taking account of the global context, trends in crucial factors influencing future developments of the competition environment in which Slovak industry will be operating in the decades to come.
3. enhancing competitiveness of Slovak industry, which can only occur provided that the two aforementioned processes have been successfully implemented and which is a sine qua non for success of Slovak industry in the world's markets.

Expectations of the public, which it formulates in relation to the whole Slovak economy and which most often include the following, cannot be deemed to be realistic until the above objectives for Slovak industry have been accomplished:

1. a marked reduction in unemployment,
2. improving standards of living,
3. improving the quality of life.

3.1.2. Basic principles

The aforementioned ambitious objectives can be accomplished provided that a new industrial policy is grounded on completely different principles than those of the industrial policy now in place. This principal shift can be outlined through a shift in approach in the following areas:

1. from isolationism to openess

From the long term perspective, the efforts to pursue economic and industrial policy in disregard of the global context, into which the Slovak economy is put, turn out today to be counterproductive and have had an adverse impact on the current status of most industries.

However, equally pernicious are also constantly present protectionist tendencies attempting to escape competition by restricting it by the state. This approach is for the benefit of neither consumers nor such protected industry or manufacturers. On the other hand, in turn, the market is distorted by unduly subsidized foreign products. Though an industrial policy must be targeted toward pushing for the concept of an open and competitive market.

Only a consistent application of this concept stands a guarantee for consumers of continuous improvement of competitiveness and quality of products and services with which Slovak industry – in the daily fight with competition – is looking to win their favour.

2. from selective direct interventions to system environment creation

In the previous periods, wrong prioritizing was the underlying cause for failure of the state policy. The state with its erroneous policy (expansionary budget policy, nontransparent privatisation) destabilised the environment and then attempted to deal with unfavourable results through inadequate interventions in the microsphere (Revitalisation Act).

The basic prerequisite for success of a new industrial policy is to reverse the order of the two approaches. The primary attention needs to be focused on systematic creation of a favourable business environment, which however cannot be provided with just a narrowly perceived, traditional industrial policy, but all of the other relevant state policies and industries responsible for their implementation must get involved in its creation. Without their close co-operation any – however well formulated – policy is bound to fail.

Unlike the past, efforts toward the selective approach, which had a demotivation effect rather than produced a positive result, will be minimized. However the system approach to the creation of a favourable overall framework for business does not fully preclude even direct interventions, but this only may be the case in warranted cases and in a predefined and transparent manner.

Where an improvement of competitiveness requires a deep-seated restructuring which might have a significant impact on employment or a marked regional dimension, also state budget funds can be used, but this being in strict compliance with EU rules on granting state aid and competition protection rules and the basic principles and conditions will be established through legislation for such measures. Widely pursued will be horizontal support policies targeted toward support for foreign direct investment, science and research, SMEs, and proexport orientation.

3. from declarations to real measures

As already mentioned, despite the objectives in the industrial policy from early 1995 more remarkable results have not been virtually achieved in this branch. Non-cohesion with the Cabinet’s financial policy was probably the biggest shortcoming of government materials on industrial policy, which basically put industrial policy just on the level of declarations with no real economic basis, and support for industry only remained in a fictitious position.

No additional measures were adopted (or those adopted were not obeyed) which would prevent corruption affairs in company privatisation, asset stripping and tunneling. Therefore the state concentrates in the next period on adopting a body of real arrangements resulting in an actual improvement of the business environment in the Slovak Republic.

4. from support for the unable and punishing the effective toward creating the conditions in support of effectiveness and pushing long-termly ineffective companies out of the market

The success of each economy, the rate of economic growth it achieves depend on its productivity, effectiveness of allocation and use of limited production factors available to it.

Economic and industrial policies in the past always devoted more attention to those industrial companies which found themselves amidst economic difficulties than those companies which achieved good economic results.

The market discipline allowing to survive only to those who produce in a more quality and effective manner than their competitors must become the basis for boosting competitiveness of Slovak industry. For those who cannot do so long-termly must face a real threat of leaving the market.

For companies posting good economic results, in turn, a favourable business environment has to be created that will not amerce them for their success but will allow them to further develop their activities instead.

3. 2. Economic challenges to Slovak industry on the eve of the 21st century

Slovakia – a small and open economy

The Slovak economy is simultaneously a) a small and b) remarkably open economy, in which the contribution of exports and imports to the GDP in 1998 accounted for 137.7 %.

A small internal market means that companies with a high growth potential – unlike their competitors emanating from larger economies than Slovakia's – have to orientate in their strategies already in early stages of their development toward gaining positions on foreign markets where they will be able to place a bigger part of their production.

A high degree of openness of the Slovak economy strengthens its dependance on exports and revenues that is able to generate through exports. This means that the performance of the Slovak economy and its industries is sensitive to external environment developments, global trends (such as liberalisation of economic relations, technological revolution or demographic trends) in the world economy at large or to developments in the Slovak Republic's major trading partners economies and in particular the EU countries economic space.

3.2.1. Globalisation and liberalisation

The ongoing globalisation of economic activities of multinational corporations and the current liberalisation of goods and capital flows constitute a factor having a significant impact on the functioning of Slovak industry.

On the one hand it implies an increased pressure on Slovak industry in the shape of the entry of international competition into the domestic market giving rise to the need to improve its competitiveness concerning costs and quality alike.

On the other hand it represents for Slovak industry an important opportunity to get involved in the international division of labour through developing subcontractor relations with large-scale multinational corporations, which at the same time means an indirect access to the world markets.

Both indicated global trends – globalisation and liberalisation – are simultaneously essentially influencing also possibilities, the method of formulation and the implementation of Slovak industrial policy. The spread of globalisation and liberalisation is increasingly narrowing room for intervention policies of that type Europe saw in the postwar period.

Removal of protectionist barriers along with the growing presence of multinational corporations, whose decision-making and managerial structures are frequently located in other countries, are limiting the possibilities of the traditional industrial policy, putting the governments of respective countries – including Slovakia – before the need to formulate a new content of industrial policy and search for such approaches as will be effective even within an environment that has remarkably changed owing to the continuing globalisation and liberalisation.

3.2.2. EU developments toward the EMU

Part of the overall trend toward removing barriers and obstacles to the free movement of production factors, posed by individual states frontiers, is also the establishment of a single market within the European Union, thus the creation of conditions for the free movement of goods, services, persons and capital.

An important external factor for the functioning of Slovak industry is even the single European currency introduction project, which is part of a broader plan for creating an economic and monetary union.

Slovakia is one of the countries seeking membership of the European Union. Both the accession process and potential membership of the EU represent a range of opportunities but also risks for Slovak industry.

Among opportunities should be included the possibility of access to the EU single market that is attractive by its size and a high buying power. In the light of access to finance for development, the EU area is attractive for Slovak industry by a higher stability – thus lower risks – compared with the domestic economy, low interest rates and, in the context of the introduction of the single currency, also the elimination of cost of converting funds into individual national currencies, which will mean a reduced transaction cost especially for larger business entities.

Nevertheless, there are also risks in connection with the Slovak Republic’s accession process to the EU. These include, inter alia, increasingly tougher competition on the domestic market, increased cost of the industrial sphere relating to the need for approximation, i.e. aligning our legislation on that of the EU. One of major potential risks is the entry into the EU of the Czech and Slovak Republic’s at different dates, which might cause complications and threaten the preferential position of industrial companies well-established on the Czech market, which is still highly important for realisation of their production.

3.2.3. Harmonisation of laws within the accession process to the EU

In implementing industrial policy, the internal market has a significant role to play. Providing the domestic market with the necessary range of products and quality may be thought to be an important part of industrial policy. It is not true at all that if the competition is taking on the form of a global competition, the importance of the internal market is lessening. All competitors require a domestic basis and thereafter expand their foreign operations from it. Positions on the domestic market stem from comparative advantages, price competition and quality. To enable an expansion even into international markets, the rules for the following areas should be accepted:

a) product standards and quality

The removal of technical barriers to trade in accordance with Articles 69, 70 and 75 of the European Agreement not only harmonisation of legal regulations and technical standards with EU regulations, but also the need to take over such procedures for demonstrating product conformity with the basic safety requirements as are in place in EU countries. A central state administration authority responsible for the issues of technical standardisation, metrology and testing line, including certification, the Slovak Office for Standardisation, Metrology and Testing Line is currently preparing a new enactment – Law on product technical requirements and on conformity assessment whereby such conditions are to be created to demonstrate product conformity with the basic requirements of technical regulations and standards as are identical to the conformity assessment procedures effective in the EU. Universally effective principles on testing line and compliance assessment will be incorporated in the law in accordance with Articles 69, 70 and 75 therein, namely:

- EC Council Resolution No. 90/C10/01 on the global approach to conformity assessment
- · EC Council Decision No. 93/465/EEC on conformity assessment modules and rules for granting the CE conformity mark
- · EC Council Resolution No. 85/C136/01 on a new approach to technical harmonisation and standards and regulations
- Directive No. 98/34/EC, as altered and amended by Directive No. 98/48/EC on providing information on technical standards and regulations
- Directive No. 92/59/EEC on general product safety, including the provisions on obligations of manufacturers and importers to place on the market only safe products

The law in point will supersede Act No. 142/1991 Coll. on Czechoslovak technical standards, as altered and amended, and obligatory product certification which is being implemented pursuant to Act No. 30/1968 Coll. concerning state testing line and implementary regulations thereof. It is the current scope of mandatory product certification in the Slovak Republic that is the source of criticism from EU experts, as it poses an extensive technical barrier to trade.

Along with the passage of the Law on product technical requirements and conformity assessment, also a Law on faulty product damage liability drafted by the Slovak Ministry of Economy is expected to be passed in 1999.

- The adoption of other EU directives in Slovak regulations concerning the free movement of processing industry products will be ensured either through autonomous legal regulations or implementary regulations to existing or upcoming acts as follows:

In relation to the upcoming Law on product technical requirements and conformity assessment, implementary regulations (Regulations) on the safety of machinery, toys, liquid fuel appliances, pressure vessels, electrical devices within the established limits of voltage and electromagnetic compatibility will be adopted in the medium-term, i.e. between 1999 and 2002. Also adopted will be a common implementary regulation for a group of so-called ”other established products”, or product groups will be selected whose conformity assessment will be regulated by virtue of special legal regulations and which will not be placed on the market until their conformity with the basic safety requirements has been assessed.

b) technical standardisation

A body of Slovak technical standards consists of some 18,500 STNs. From industries´ point of view, 14,600 standards or so, i.e. over 80 %, are either directly or indirectly related to their operation. In introducing a ”new approach”, which is based on the non-binding nature of technical standards harmonised with technical regulations, the takeover of the European standards (ES) linked with of the White Book Phase 1 Directives will be underpinned even in the conditions of industries.

As of 1 April 1999, 7,405 ESs and 2,800 ETSs were issued in European standardisation organisations CEN and CENELEC. Of this, 1,487 ESs and 534 ETSs have been introduced into the STN body, which accounts for 22.1 % of the total ES number. To meet the condition for Slovakia´s joining the CEN and the CENELEC, at least 2,500 ESs should be annually introduced into the STN body by the end of 2002.

c) testing line, accreditations and certifications

With the birth of an independent Slovak Republic, the requirement arose to build up the state testing line such that it covers all the products designed for mandatory approval and certification. From the 11 state testing shops in 1993, there currently are 28, of which 13 fall within the province of the Slovak Economy Ministry. Testing line at present constitutes a major part of bodies and organisations for the consumer´s protection against dangerous products.

d) industrial and intellectual property

According to a maintained analysis on patent and licence activity of Slovak companies, the share of domestic patent applicants and owners has been constantly dropping. The reason is first of all a low innovation level of development, the division of companies and related cessation of industrial-legal protection departments. Also financial intensity of industrial-legal protection, especially abroad, adds to said factors.

To improve the current status and boost activities in the area of creation and protection of technical creative activity results under branch technical policy, in co-operation with the appropriate central state administration authorities (ÚPV SR, MŠ SR), it will be necessary to:

- direct activity of the industry scientific-research basis in intellectual property protection within the framework of international scientific-technical co-operation, in particular in projects solved under the EU 5th Framework Research and Development Programme.
- pursue activities in the area of technical creative activity result protection as one of the criteria in assessing (accrediting) industry R& D basis workplaces.
- introduce a regular award of the ÚPV SR Chairman for results of extraordinary valuable technical creative activity, even in relation to results attained on this front in industries.

e) quality policy

In this field, conceptual objectives of industry technical policy will follow the developed National Quality Programme until the Year 2003 which takes account of not only technical issues but also economic and social issues.

The National Quality Programme until the Year 2003 is closely interlinked with the European Quality Programme, taking into consideration its primary activities targeted toward raising motivation, human potential development and providing cohesion between all entities engaged with the creation of quality and position of the Slovak Republic in the world.

3.2.4. Technological changes

The ongoing revolution in the area of information and communication technologies has the effect of bringing about a fundamental transformation of economic and societal life, which is consequently influencing all industries.

Due to revolutionary developments of information and communication technologies, not only ways of communication are outright changing, but a variety of new economic activities based on information and communication technologies are emerging, new jobs are arising, traditional work procedures are changing, the comprehension of the essence of the very work is undergoing a literally revolutionary development.

Similarly in the field of biotechnologies, it is going to influence at least in the next decade several industries, in which existing manufacturing technologies and procedures will be replaced with new biotechnologies.

Modern technologies are for industry not only the source of higher productivity and quality of production and services provided, but also a challenge to undertake substantial changes in the organisational structure of individual companies. Developments are proceeding toward constantly enhancing flexibility and strengthening a tailored approach to customers that will become key competitiveness parameters.

Because of the technological revolution even industrial companies are opening the possibilities of replacing large numbers of the same products with a more diversified production which will be capable of better meeting the requirements of individual clients.

Under the new international division of labour, the production of large numbers of unified products of standard quality is progressively shifting toward – mostly developing – countries with lower production cost. Competition on this market segment is becoming more intense, as more and more countries can produce with low labour cost large numbers of relatively quality industrial products.

In advanced countries, there is a shift taking place from large-scale productions toward productions featuring high quality. Skilled labour and its ability to absorb and thereafter bring to bear new knowledge in the production process rather than price or production size as was the case in the past will be increasingly becoming the principal barrier to the entry into this market.

In order for Slovak industry to catch up with the trend, it is necessary in terms of industrial policy to take account of it in the educational system and the labour requalification system. From the perspective of individual industrial companies, the capacity of their management to identify the needs of the world market and adapt technological equipment and qualifications of own staffs will be key.

Slovak industry and the whole Slovak economy will depend for the future rate of growth on industry's capacity to get involved in production and provision of services in the above areas, thus being competitive in them.

3.2.5. Changes in the labour pattern and organisation

The labour pattern with respect to its age composition is and will be significantly influenced over the following decades in particular by demographic developments. Anticipated developments in the age pattern, which will be characterized in the decades to come by a fall in the share of productive-age population and a considerable increase in the share of post-productive-age population, represent an increased financial burden on income systems.

On the other hand, however, these developments pose a challenge to reevaluate the traditional view of employment of an individual during his/her life cycle. The permanent extension of life span is the opportunity to remove formal restictions (official retirement age) while defining the productive and post-productive age.

Major changes are also occurring in employment in the light of sectoral pattern of industry, the share of women of total employment and labour qualifications.

Said trends – i.e. mainly the persistence of higher age brackets of the population in the labour category – will be creating pressure to bear on growing unemployment. It will only be possible to cope with such developments provided that innovative approaches to labour organisation will have been adopted on time.

Even the aforementioned revolutionary changes in technologies are being reflected in the labour pattern and organisation. Developments in advanced nations are clearly proceeding toward fundamental changes in employment. All-important changes include individual self-employment, a reduced working week as well as more flexible forms of employment based on partial work contracts, 1 job – 2 employees schemes, etc.

These changes are also related to the global trend from old, hierarchically organised methods of labour organisation toward new, modern and flexible – business – approaches placing a premium on the spread of the foregoing flexible forms of labour.

Fundamental changes in the labour pattern and organisation thus will be one of the key factors which Slovak industry has to get to grips with, if it is to successfully compete with its production on the world market.

3. 3. Analysis of Slovak industry competitiveness and performance

Slovak industry competitiveness is one of the key factors for successful integration of the Slovak economy into the EU.

Slovak industry is an important branch of the Slovak economy in terms of its production, employment, but particularly in Slovak exportation terms. The contribution of industry to the GDP in 1998 stood at 26.7% (in current prices), with industry employing 30.2% of all the employees in the national economy.

Of 318.3 billion Sk worth investment acquired in 1998, the share of industry was 39.5 %. Foreign capital into individual industries came in 1998 to 35.6 billion Sk, which is 51.1 % off total foreign capital invested in the Slovak Republic by the end of 1998.

With its 77.8 % share in 1998, the private sector has currently a crucial weight in total production of industry. According to the Slovak Statistical Office, 9,196 business entities, including small enterprises with up to 20 employees, were registered in Slovak industry as of 31 December 1998. Additionally, tradesmen with total average staffs of 72,893 for 1998 are doing business in industry. The average number of employees in Slovak industry in 1998 was 583,886 (including small enterprises with up to 20 employees and tradesmen), of which 93.3 % worked in industrial production, 8.3 % in electricity, gas and water generation and distribution and 3.4 % in mineral mining. 82.5 % of employees work in enterprises with staffs of 20 or more.

Trends in basic indicators for industry between 1994 and 1998

Table

Goods production in Slovak industry, year-on-year changes, %

(organisations with 20 or more employees)

	1994	1995	1996	1997	1998
Ťažba nerastných surovín	-4,6	-0,3	5,6	7,5	-20,7
Industrial production	1.7	9.6	2.2	2.2	7.4
Electricity, gas and water generation and distribution	15.9	-2.0	5.0	- 4.0	- 5.1
Total industry	3.0	7.4	2.6	1.7	5.4

Source: Slovak Statistical Office

Following a relatively buoyant growth in industrial production in 1995, the succeeding years has seen a decline in growth dynamism.

The production of means of transport contributed most to the tendency toward increasing the industrial processing production share of total industrial production, doubling its share between 1995 and 1998 and standing in 1998 at 14.4% off total industrial production. Currently providing 5.6 %, the production of electrical machinery and equipment also showed a tendency toward increasing its share of industrial production. A downward trend in the industrial production pattern share had been recorded for the food production, textile and garment production, leather processing and leather products, and last year also for the chemical production.

Slovak industry's core branches are the machine (car manufacture), food, metallurgical, chemical and power industries.

3.3.1. Analysis of competitiveness of processing industries in the light of export performance

The underlying problem of Slovak industry in export terms rests in that Slovak industry has the largest comparative advantages in SITC commodity groups 6 and 8, thus in semiproducts and simple finished products whose 1996 share was 50 % off total exports. In hitherto developments, there is a strong share of industries featuring a lower degree of procession and high raw material, energy and transport intensity. The product pattern is dominated by subcontracts, semiproducts and simple consumer products, and production finalisation is lagging far behind.

Industrial companies are holding a crucial share (approx. 80%) of Slovak exports. In 1998, the export sales share of total sales for industrial companies accounted for 40 %. The production of double track motor vehicles is contributing most among the industries toward both export sales in absolute terms and its growth dynamism. Its 61,047 million Sk worth sales posted for 1998 are nearing a fourth off total export sales in Slovak industry (23.4 %) and is by far outperforming such former traditional export productions as chemical, metal, and machinery and equipment production.

Nevertheless, Slovakia is achieving in foreign trade a relatively low foreign exchange effect and must export relatively higher quantities of goods to pay for realised imports, since exports are dominated by commodities displaying low procession degree, high capital, raw material and import intensity.

On the front of processing industry product imports, these had been increasingly contributing over the period followed toward meeting the domestic needs, in particular due to high market liberalisation on the import side as well, low customs barriers, tough competition from foreign firms. Such developments resulted in year-on-year growth in production imports progressively outstripping that in exports and consequently an aggravating foreign trade balance.

This is clearly suggested by foreign trade developments for processing industries between 1995 and 1998 as indicated below:

(billion Sk)

INDUSTRY	1995			1997			1998		
	export	import	bal.	export	import	bal.	export	import	bal.
Machine	42.6	67.1	- 24.5	75.7	117.3	- 41.6	116.9	153.5	- 36.6
Electrical	11.6	18.3	- 6.7	22.6	39.6	- 17.0	29.3	50.1	- 20.8
Chemical and pharmac. ind.	50.8	43.2	7.6	49.1	52.1	- 3.0	49.8	64.0	- 14.2
Wood-making industry	47.0	18.4	28.6	52.3	24.7	27.6	55.2	30.7	24.5
Light industry:	30.2	15.6	14.6	44.8	30.9	13.9	47.2	41.4	5.8
of which: textile and garment	17.9	9.8	8.1	27.7	19.7	8.0	29.6	2.3	3.3
Leather and footwear	5.2	2.8	2.4	8.8	6.6	2.2	8.7	8.0	0.7
Publishing	2,5	1.4	1.1	3.2	2.7	0.5	3.7	4.3	-0.6
Glass-making	4,6	1.6	3.0	5.1	1.9	3.2	5.2	2.8	2.4
Food industry	5,9	12.3	- 6.4	7.0	15.8	-8.8	6.8	17.3	- 10,5
Total processing industry	188.1	174.9	13.2	251.5	280.4	- 28.9	305.2	357.0	- 51.8

Customs statistics data

The foreign trade balance in individual processing industries between 1995 and 1998 had been influenced especially, but not limited to, by the following commodities:

· in the machine industry, despite proexport orientation of the product pattern, high imports of machine industry products for the needs of the entire national economy and manufacturing capacities not utilised up to 100 % all had an adverse impact on growth in adverse foreign trade balance (in 1995 through 1997). In 1998, it dropped owing to a marked increase in motor vehicle exports

The foreign trade balance was influenced:

- on export side: - was positively influenced in particular by growth in exportation of motor vehicles, rolling stock, central heating steam boilers, ships and boats;

- on import side balance developments were influenced in particular by growth in importation of boilers, nuclear reactors, motor vehicles and parts thereof, rolling stock, aircraft and parts thereof;

In this industry, there are no barriers to the free movement of goods except for defence equipment.

The machine industry, excluding strategic enterprises, is privately owned. Of importance is also the presence of foreign capital in the automotive industry and white equipment production.

- in the electrical industry a adverse balance of trade in 1998 of up to 20.8 billion Sk was influenced:

- on import side: - in particular by importation of information technologies and automatic data processing machines for the needs of the national economy;

- on export side: - by a remarkable increase in exportation of radio, television and communication devices (OKEČ 32) and by exportation of electrical machinery and equipment (OKEČ 31).

Under the White Book Sector 2 ”Free Movement and Safety of Industrial Products” works on harmonisation of Slovak legislation with that of the EU fall within the province of the Slovak Office for Standardisation, Metrology and Testing Line. Certification issues in the branch are provided by state testing shops (notably EVPÚ Nová Dubnica, TSÚ Piešťany).

The electrical industry has been privatised since 1995. Foreign capital entered the electrical industry through major projects (Siemens, SONY, ALCATEL SEL, Motorola, Bull, ABB, OSRAM and others) and this trend in foreign investment inflows is expected to continue over the next period too.

- in the chemical and pharmaceutical industry, an active foreign trade balance of 7.6 billion Sk in 1995 turned into an adverse balance of 3.0 billion Sk in 1997 and shot up in the course of 1998 (to – 14.2 billion Sk). Over the period, foreign trade balance for the chemical and pharmaceutical industry was influenced: on export side in particular through the maintenance of or a moderate drop in exportation of rubber and plastic products, organic chemicals, resins, pastes and chemical fibres;

- on import side there was a marked rise in importation of medicines and substances, consumer light products, plastic products and anorganic and organic products.

- From the perspective of foreign trade, the openess of the chemical and pharmaceutical industry is relatively high for both imports, which are highly liberalised in the Slovak Republic, with low customs barriers, so domestic chemical and pharmaceutical face strong competition from foreign firms, and exports whose share of total sales ranging from 63 to 64 % measures up to advanced states.

Chemical and pharmaceutical product imports are increasingly contributing to satisfying the internal market needs, namely in particular in the subbranch of chemicals, chemical products and fibres above all in the area of chemical specialties, consumer chemistry and medicines, where the product range is highly diversified and the product range offer is being expanded in connection with chemical products for specific purposes. Homegrown products are in a dead heat with competition, especially from Western European firms, also because the product range offer from domestic producers is lacking. Still, given growing manufacturing capacities in connection with their effectiveness and a relatively tiny domestic market, it is not economical to fully secure their demand through domestic production.

Exports are mostly headed to the Czech Republic and EU markets. Imports are dominated by EU suppliers and the grouping's share is gradually rising. Ag goes the pattern of exports especially to the EU, these are dominated by products having lower added value. The market of the other CEFTA countries is progressively gaining importance.

Of product groups, chemical fibers appear most competitive, even if their competitiveness is aggravating in connection with a surplus of fibers on the Western European market relating to the crisis in Southeast Asia. With respect to mineral fertilizers, competitiveness has been influenced by lower-priced fertilizers from Ukraine and the Russian Federation and a drop in the price of natural gas on the world market and consequently also fertilizers prices on the Western European markets, while the natural gas price for Slovak fertilizer makers is regulated and when converted into energy unit is higher than with Western European fertilizer makers.

· in the woodworking, furniture and pulp-paper industry, active foreign trade balance is provided in the period followed, albeit it shrunk (from 28.6 billion Sk in 1995 to 24.5 billion Sk in 1998).

Foreign trade balance developments were influenced:

- on export side, in particular by growth in exportation of wood and timber, building joiner's and carpenter's products, paperboard and veneer board, wooden and upholstered furniture and parts thereof, system buildings, chemical wooden pulp, painted and non-painted paper, cardboard and pressboard, toilet paper,
- on import side, in particular by growth in importation of building joiner's and carpenter's products, wood particle boards and fiberboards, wooden and upholstered furniture, painted and non-painted paper, cardboard and pressboard.

The dissolution of the domestic market together with a stopped housing development and minimized exports into the Russian Federation had also an adverse impact on the performance of the woodworking industry but first of all furniture industry. By lowering finalisation the realisation of wood fell by 25 to 30 %. An adjustment 12,000 to 14,000 Sk per 1 m^3 of wood when converted into the 1995 price level was achieved in 1990, whereas it was as low as 9,000 SK in 1997.

Even despite these facts, exports for the woodworking and furniture industries hold over a 50 % share and the pulp-paper industry an impressive 64 % share of total sales, which bears evidence to high competitiveness of the production.

Imports into the branch are effected in the form of materials and other components for industrial consumption. From this perspective, the branch import intensity is below 30 %, which could be further reduced provided that productions based on disintegration of the remaining product ranges of raw wood are developed.

Woodworking, furniture and pulp-paper product imports over the period are increasingly contributing to meeting the domestic needs (from 18 billion Sk in 1995 up to 31 billion Sk in 1998). In spite of this, an active foreign trade balance is provided throughout the period, while there was a drop in it.

· in the light industry, an active foreign trade balance is provided throughout the period with its progressive decline (from 14.6 billion Sk in 1995 to 5.8 billion Sk in 1998). The light industry comprises the textile, garment, leather and footwear, publishing and glass-making industries.

Foreign trade balance developments were influenced:

- on export side by a rise in textile and garment product exports, glass products, leather products and footwear,
- on import side by a rise in textile and garment product imports, including basic input raw materials. There was also a considerable increase in imports within the publishing industry goods pattern (drawing documentation for investment units).

One of competitiveness criteria for the light industry is its export performance, which is obviously higher than in total industry. The 1998 share of export sales came to 47.8 %.

From the perspective of ownership relations, it can be noted that privatisation in the branch has been in fact completed, save two entities. While foreign capital is active in all branches of the light industry, its inflows are not yet up to the level necessary for branch development.

· in the metallurgical industry, in terms of basic production-technological processes, product range and quality, the state is comparable with the EU metallurgy, which is borne out by permanent sales of over 70 % off production on foreign markets.

Our market with steel is fully liberalised already for the very reason that the absence of the manufacture of long products as well as of the entire range of products from alloyed steels is fully offset by imports from CEFTA states – primarily the Czech Republic, and the permanently rising share of imports from EU countries. It bears recalling that competitive flat products from Ukraine and Russia have been thrusting their way into our market of late.

By allowing the full privatisation of steel and iron metallurgy, the state virtually renounced any control over management of this significant branch, which is even in economically advanced states the subject of a prudent procedure of ownership transfer. The Slovak Government seeks to handle the hitherto economic plight at VSŽ, a.s., Košice through equities held by Slovak banks and the Slovak National Property Fund (FNM SR) with no direct interventions in the management of the VSŽ workings and negotiations with potential foreign strategic partners.

- power engineering and mining industry

In the field of oil products, Slovak products are competitive, products from power plants and Slovenský plynárenský priemysel gas company are not designed for export, or exports/imports are only effected as short-term financial transfers to provide the balance of sources and needs. The quality of electricity supplies is assured by way of observing standards, dispatching load control as well as connection with the UCPTE system. The Slovak Republic ratified the Convention on Energy Charter providing for non-discrination conditions for energy investment, the free movement of energy goods.

A major foreign exchange source is the largest European transit system in capacity terms to carry natural gas from Russia over to Central and Western European countries.

Business on the non-discrimination principle is sufficiently allowed by a new Act on Power Engineering (except for free access by third parties to grids).

Direct public subsidies are granted for: heat supplies from CZT systems, sorted types of brown coal for the population, law-mandated benefits to miners and social mining at Baňa Dolina Veľký Krtíš (maintenance of employment).

Electricity and natural gas prices for households are indirectly - cross-subsidized (from the business sphere).

A proposal for abrogating Act of the NC SR No. 192/95 on the provision of state interests in privatising strategic enterprises, which did not allow to privatise the property of crucial power companies SPP, ZSE, SSE a VSE, nor the shares of SE, a.s., and Transpetrol, a.s., is currently going through the legislative process.

By concluding this section, it can be noted that the ongoing transformation process in trade flows has set off Slovakia's position as an open economy. And this on both the export side and import side. Exports and imports of goods and services (total turnover) totaled in 1995 a mere 124.7 % off GDP, in 1998 up to 137.7 % off GDP, this ratio however reflects also a low performance of the economy expressed by the GDP. Pritom:

- export performance (export of goods and services to GDP in current prices in %) achieved some 63.4 % off GDP in 1998 (only 0.4 % up on 1995)

- import intensity (import of goods and services in current prices in %) achieved 73.4 % off GDP in 1998 (as much as 13.1 % up from 1995).

The foregoing suggests:

- a high increase in imports, not adequately covered after 1995 by the economy export performance, which manifested itself in growing debt, currency depreciation and increased inflation,
- a low export performance and a high propensity to import, which represents one of the basic structural-performance imbalances of the Slovak economy. This imbalance is closely related to the economic situation in the light of existing industrial capacities, where, on the one hand, the raw material and energy intensive structure of these capacities is putting high demands on the import of material and energy inputs and, on the other hand, the scope of their potential production multiply exceeds the domestic market absorption possibilities.

In relation to the above, industry and within it the processing industry play a key role, because industries (in particular machine, chemical and pharmaceutical industries and pulp-paper industry, whose share of total industry exports accounted for 56 % (and for the processing industry as much as 61 %) in 1998, are making a considerable contribution within the industrial production structure and meeting foreign demand.

3.3.2. Analysis of Slovak industry financial performance

Retained earnings

The results attained on the front of management and effectiveness show an adverse trend. Retained earnings generated by industrial companies totaling 4.4 billion Sk only represents 28.9 % off that made in 1997. Branches (processing) as a whole posted a loss of 8.4 billion Sk. The amount of bank loans and short-term financial transfers increased, trade accounts payable totaled 234.9 billion Sk as of 31 December 1998, of which overdue obligations 76.7 billion Sk with a year-on-year increase of 18.1 %. Overdue obligations outstrip outoverdue receivables in industry by 6.3 billion Sk.

Endebtedness

The financial situation of industrial companies is expressed to a certain extent by the state of indebtedness, i.e. equity / debt ratio (obligations toward banks and suppliers). Equity of industrial companies totaled 419 billion Sk as 31 December 1998, the sum of bank loans and obligations 429.2 billion Sk. Of the 2,049 reporting units in Slovak industry in 1998 (statement P 3-04), nearly one half of the units (49.6 %) has debt higher than equity, 308 units post even a negative equity. These companies bear all the symptoms of bankruptcy and meet the criteria for instituting bankruptcy proceedings. Their sustentation is drawing more and more entities into the environment of insolvency and payment non-discipline. The indicated number of ”insolvent” companies employ 199,611 staffs with 281 billion Sk worth revenues.

Insolvency

By comparing the state of and trends in insolvency, a certain picture of the financial position of companies can be obtained. To assess developments of insolvency expressed by overdue obligations and receivables, the data obtained through statistical survey from quarterly statements P 3-04 to be submitted by organisations with 20 and more employees (until 31 December 1996 with 25 and more employees). These are both short-term and long-term obligations and receivables, trade accounts payable and receivable, toward government, social and insurance funds, without obligations toward the banking sector.

The branches falling within the province of the Slovak Economy Ministry saw the following trends in overdue obligations and receivables:

Table

Overdue obligations, million Sk

Branches by sectoral category of economic activity		state as of:				
		1 Jan. 95	31 Dec. 95	31 Dec. 96	31 Dec. 97	31 Dec. 98
C	Mineral mining	1,439	691	749	1,548	1,347
D	Industrial production	47,597	47,931	53,890	60,294	68,287
E	Electr., gas and water gener.	5,337	5,511	2,560	3,074	6,672
	Total Slovak industry	54,373	54,133	57,199	64,916	76,306
G	Trade, motor vehicle repair	13,387	11,230	11,092	18,029	22,284
H	Catering and accommodation	318	358	502	753	989
T o t a l		68,078	65,721	68,793	83,698	99,579

Table

Overdue receivables, million Sk

Branches by sectoral category of economic activity		state as of:				
		1 Jan. 95	31 Dec. 95	31 Dec. 96	31 Dec. 97	31 Dec. 98
C	Mineral mining	1,193	1,039	834	1,288	1,640
D	Industrial production	47,603	54,927	53,859	53,273	54,867
E	Electr., gas and water gener.	9,100	10,870	5,512	6,891	15,921
	Total Slovak industry	57,896	66,836	60,205	61,452	72,428
G	Trade, motor vehicle repair	17,729	15,184	16,777	20,876	28,782
H	Catering and accommodation	185	191	259	273	293
T o t a l		75,810	82,211	77,241	82,601	101,503

A further growth on the previous years follows from the data on insolvency aggregated by individual branches. A ratio of overdue obligations for industry to overdue obligations for the Slovak Republic came to 56.6 % as of 31 December 1998. For overdue receivables, this ratio is 52 %. We see its cause in addition to the poor financial and payment discipline of companies cited above also in the adverse conditions for getting loans for business entities. The rise in the amount of overdue obligations is the businessmen's response to the borrowing price and nonavailability.

A flagging financial performance of industrial companies thus limits their possibilities to finance their development through own resources, which in turn reduces their margins of manoeuvre in boosting their competitiveness.

Problematic areas common to a range of companies of several industries can be identified as follows:

- poor financial liquidity of manufacturers
- financial provision for production outsourced
- sales non-provision for production
- incomplete property transformations
- absence of strategic partners to restore technical and technological levels
- poor quality of the whole production process
- technological obsoleteness
- lack of own investment resources
- increased financial cost
- costly borrowing
- insufficient level of corporate management

3.4. A need for a deep-seated and sweeping restructuring of Slovak industry

3.4.1. EU trends in industrial restructuring

The primary objective of restructuring is to eventually improve the corporate sphere's economic viability. From this point of view the cost of successful restructuring for the state budget is by far lower than the cost of upkeeping non-viable industries.

In most EU countries an opinion currently prevails that the industrial restructuring is in the first place the responsibility of the corporate sphere, the state role is to create a good business environment and a stable institutional and legal framework.

The government and public authorities are to be just a coordinator for the restructuring processes, their role is to ”facilitate” rather than ”finance” the necessary changes. Though the responsibility for the change itself lies with the industry proper.

Arrangements implemented in certain European Union members states (e.g. the UK, France, the Netherlands – mining, steelmaking restructuring, Portugal, Spain – textile industry restructuring, Ireland – success in courting new industries) are often cited as examples of successful restructuring.

Nevertheless, a lesson should be also learned from the mistakes made by EU countries in the past, their efforts to select the ”winners”. Such an approach should be abandoned. Arrangements to be avoided are as follows:

1. significant assistance to non-viable industries and companies (Sweden or the Netherlands may serve as negative examples in granting assistance the shipbuilding industry),
2. introduction of market distorting mechanisms (protectionist measures, safeguarding a monopoly position and rights),
3. competition distortion (e.g. by building new companies through public funds)
4. granting subsidies not restricted in volume and time,
5. subsidies to and bailing out companies without commensurate obligations in relation to production restructuring.

On the other hand, the following are government arrangements and initiatives referred to as most appropriate:

1. education/training, requalification, improving managerials skills, PS and population skills

2. SME development, employment support in other industries, especially in the regions affected by restructuring

3. improving the infrastructure and ecology

4. support for research and development and quality policy

5. stressing the regional aspect of said arrangements.

Thus in the EU there is relatively broad – aforementioned – agreement on the role of the state and the corporate sphere in restructuring, but a consensus is less obvious with respect to instruments and universality of EU countries´ experiences for specific conditions of CEE countries.

Opinions varies in particular on the question whether or not the state should provide financial assistance to troubled companies. In certain countries an opinion prevails that none assistance should be granted and, if any, so only for: 1. a company's departure from the market, 2. facilitation of an early retirement of restructured companies staffs. In other countries, in turn, a belief is more widespread that the state should actively use such restructucturing instruments as credits, budgetary measures, reduced interest rates, bailout, etc.

All told, however, it can be noted that while the origin situation varies in different countries, methods of remedy are the same.

Experience of other countries show that the less intense state aid the lower risk of funding non-viable companies. The cost of successful restructuring for the state budget is lower than that of upkeeping non-viable industries. Successful restructuring represents savings, not additional cost for the state budget.

3.4.2. Criteria for assessing the viability of industrial companies

When measuring the effectiveness - thus viability – of industrial companies via statistically recorded data, the most often problem is the choice of the most appropriate methods, which is further complicated by special conditions of the Slovak economy.

It is apparent from the previous sections that a bulk of Slovak industrial companies are loss-making, essentially different from advanced market-driven economies where a bulk of business entities are profit-making.

As already cited in the introduction, a company´s loss-making in conditions of the Slovak economy may frequently results from a destabilized environment, which is a grave difference between the Slovak economy and relatively stabilized advanced market economies.

It is therefore of high importance to make distinction, on the one hand, between the companies posting a bad economic result due to their own ineffectiveness and poor competitiveness and, on the other hand, the companies whose economic result is indeed negative, yet in a normal – stabilized – environment they would be viable.

From this point of view it is felt appropriate to use the criteria recommended by the World bank. The essence of this procedure is to put the companies in four categories (see Fig.):

Category A: companies making profit safely covering all costs

Category B: companies whose revenues cover operating and labour costs, but fall short of repaying financial cost

Category C: companies whose revenues cover operating cost, but fall short of fully covering labour cost

Skupina D: companies whose revenues cover neither operating nor labour costs.

The number of companies put into respective categories may be established based on the rate of occurrence of firms by % profitability.

At the same time the above classification offers a criterion to assess the viability of companies. ”A” zone companies are troublefree and require no special aid. Equally clear is the situation with companies falling within category ”D”, where the departure of a company from the market: bankruptcy and subsequent winding up is the only correct solution in the light of market protection from adverse influence of the spread of obligations / receivables. ”B” and ”C” zone companies are the potential target of restructuring.

3.4.3. Slovak industry restructuring

The Slovak economy had been built in the past such that it could produce the widest possible range of products and services. As a result, it produced – and to a considerable extent it still does – almost everything, literally from ”locomotives through to needles”.

Obviously, this state is not sustainable in the long term for a small economy. It has to shift the limited resources available to it toward a reduced number of areas. The Slovak economy must change its way of involvement in the international division of labour and specialize more remarkably.

As regards the identification of the industries and fields in which the Slovak economy has an competitive advantage, this process cannot be dogmatically reduced only to those hi-tech industries, science and technology intensive industries, only to the production of sophisticated products. A comparative advantage can be also achieved by introducing more sophisticated procedures in the production of relatively low sophisticated products.

Role of the state and the corporate sphere in the restructuring process

Based on trends dominant in EU countries as well as based on own experience from the past, the role of the state in the process of restructuring Slovak industry is to:

1. bring home to all the parties concerned that restructuring is a necessary alternative to total collapse of non-restructured industries,

2. develop a restructuring programme,

3. put all required legislative changes in place,

4. coordinate and monitor the introduction of restructuring arrangements.

Beside creating the conditions for reduction of redundant activities and release of capacities and labour from non-productive areas, the state bears the responsibility for creating a competitive environment for restructuring activities such that these are undertaken on a level of each individual company.

Competitiveness is not something static, it is a dynamic quantity instead. What is not competitive today, it may be competitive tomorrow and vice versa. Each company has competitive and non-competitive parts.

The state has to form such institutional and legal framework as will motivate each company through both positive and negative incentives to separate competitive activities from non-competitive. A competitive part will stand better chances of attracting foreign direct investment, a non-competitive part must be dissolved in a socially acceptable manner.

Identification of the basic barriers preventing the restructuring process from stepping up as well as proposals for the introduction necessary legislative and institutional changes are addressed by a special material ("Analysis of Insolvency in the Business Sphere and a Proposal for Corporate Financial Restructuring", Slovak Finance Ministry), in the preparation of which also Slovak Economy Ministry officials heavily participated and accordingly there is no need for giving details here.

Ameliorating access of companies to operating capital

The key current problem of Slovak industry is the lack of operating capital for those industrial companies which have outsourced production, trading partners, secured sales, but which have no access to finance to purchase production inputs because of their current high debt, undercapitalisation, or combined debt and undercapitalisation.

The role of a financial intermediary for this type of company is traditionally played by development and risk capital. This brings in not only finance but also consultancy in financial restructuring, setting a good corporate strategy, marketing strategy, market analysis, establishing commercial contacts, improving the management of company top managers, etc.

Of key importance however is providing capital through majority or minority holdings, which is aimed to upvalue a company in the medium term. It is important that such a kind of capital usually attracts also significant institutional or strategic investors.

The state may be instrumental in this area not only through a stabilization policy within the macroeconomic framework that will be conducive to lowering interest rates, but above all through the creation of favourable conditions for a more massive entry of institutions that will intermediate resources to fund operating capital.

Access to resources of Slovak industrial companies to finance their restructuring and development objectives can only improved through meeting the expectations of investors who have development and risk capital, which include especially, but not limited to:

1. removal of institutional and legislative barriers and thereby creating better conditions for risk capital,
2. amelioration of the tax regime relating to risk capital
3. creation of conditions for long-term capital resources
4. support for trade of minor companies with high growth potential on the stock exchange.

Establishment of an information system on the quality of corporate assets and liabilities

However a prerequisite is a substantial increase in the scope and quality of information on Slovak business entities, quality of their assets and liabilities, profitability, corporate management quality, ownership structure, since it is unthinkable to talk about attracting a bulk of foreign resources until such a condition has been met.

One of the basic conditions for successful progress of restructuring is the establishment of an information system on the quality of assets and liabilities, which will be providing information in the pattern common in terms of international scope in Slovak and English alike.

Still, it is unthinkable to set it up and put into operation without responsiveness from the owners and managements of individual companies in furnishing information concerning the management of their companies.

The quality of information, which is to be available as widely as possible, is also a key factor determining as to what extent the secondary market with receivables can get off the ground. Its goal is to streamline and cut the unduly lengthy and costly process of converting receivables into cash and subsequent formation of majority holdings in companies, which are required for effective exercise of titles.

3.4.4. Shifting activites toward new areas

Restructuring however does not only mean the cessation of ineffective companies and industries but at the same time also a shifting economic activities toward new industries and areas.

As already noted above, Slovak industry is characterised by a strong dependance on traditional industries, on the one hand, and too low a share of modern industries, on the other. This statement is also borne out by the following table showing a contribution by these industries to total production and employment in industry.

Contribution of selected industries to employment and production in industry in 1998

	Goods production(%)	Employment (%)
MODERN BRANCHES		
Production of means of transport	14.37	5.45
Production of machinery and equipment	6.49	13.41
Production of electrical and optic equipment	5.96	7.96
Production of pharmaceutical preparations	1.41	1.00
TRADITIONAL BRANCHES		
Production of metals and metal products	15.29	11.74
Production of foods and beverages	12.98	10.13
Prod. and distrib. of electr., steam and water	9.64	9.65
Production of chemicals, chem. pr. and fibres	6.97	5.07
Production of coke, ref. pr. and nuclear fuels	6.13	1.06
Production of pulp, paper and cardboard	5.21	4.14
Production of non-metal. min. products	4.13	5.20
Production of rubber and plastic products	3.26	2.93
Textile and garment industry	2.85	9.75
Production not classified elsewhere	1.96	3.31
Mineral mining	1.86	4.05
Woodworking and wooden products	1.48	2.63

The countries which restructured their industries in the past have succeeded mainly because they managed to shift their production capacities toward areas that are perspective even in the new millenium.

Slovakia's specific is the fact that industrial policy has to be implemented in the situation where much of the economy has to be subject to restructuring.

Under this situation, also the application of sectoral programmes can be considered to help the industries that need to undergo restructuring (e.g. mechanical engineering, mining, metallurgy, textile industry, woodworking). If such an instrument is used, it will be done so in strict compliance with the EU rules on granting state aid and the competition protection rules.

Within the creation of a legal framework for granting state aid in the Slovak Republic, a bill on state aid has been drafted, taking over the key elements of Articles 92 and 93 of the Treaty establishing the EC, basic principles and conditions for granting and monitoring horizontal, regional and sectoral state aid. Part of the bill are also the provisions on granting state aid for the automotive, steel and shipbuilding industry and man-made fibres. The purposes for state aid and limits thereof for the established areas have been proposed such that they are in line with relevant EU directives including the set-up of an office for state aid. The bill is expected to be approved by Parliament by late September 1999.

A gradual adaptation of industrial structure to the EU accession conditions is of necessity, and the Slovak Republic has expressed in accordance with the economic criteria contained in the National Programme for Acceptance of the Acquis Communautaire, approved by UV SR No. 427 of 26 May 1999, interest to develop mechanical engineering targeted toward the automotive, electrical, information technology industries, light chemistry, woodworking, paper and publishing industries.

The primary priorities of industrial policy include – besides the creation of a favourable business environment and launching restructuring – providing for smooth transfer of redundant production capacities and labour being released to new areas.

The state may largely contribute to this by bringing to bear horizontal programmes to encourage foreign direct investment inflows as well as support SMEs.

3.4.4.1. A need for other measures to attract FDI

From the perspective of relations of Slovak industry toward large-scale strategic companies (e.g. Volkswagen) already active in Slovakia, it should be noted that potential for mutual co-operation has not yet been delivered by far.

One of the basic strategic goals of industrial policy in this area remains even into the future to strengthen and more closely interlink foreign investors in the Slovak Republic, on the one hand, and their Slovak subcontractors, on the other hand. This way of developing economic co-operation between domestic and foreign companies is a suitable form of getting involved Slovak industrial companies in the organisational structures of giant multinational corporations and their indirect entry into the world markets, which however envisages the observance of contractual obligations and in particular of high quality standards by Slovak suppliers.

It is likewise necessary to deem gaining of new strategic investors for industries to be the underlying strategic priority of Slovak industry and the state industrial strategy. Be it investment into existing companies or ”green meadow” investment, the Slovak Republic has to court it in the face of tough competition from the neighbouring countries.

From this point of view, the hitherto offer available to foreign investors, made up of a combination of such parameters as site, labour price and quality, tax and other financial allowances and full access to the EU market, should be critically reassessed.

Adopted in March 1999, a strategy to encourage foreign direct investment should be perceived in this context just as the first step toward lessening the Slovak Republic’s lagging behind the neighbouring countries with respect to creating favourable conditions for business.

It should be openly noted that even after adopting the strategy and certain partial measures (e.g. an amendment to the Income Tax Act which took effect 1 April 1999) the Slovak Republic does not measure up to the Czech Republic, Poland, Hungary or Slovenia, because also these countries have made dynamic progress in this area.

The foregoing suggests an urgent need for other arrangements to attract FDI which should come over within the shortest possible window of time and which should be targeted at least toward removing distortions and discrimination provisions that tainted the cited FDI support strategy.

It is particularly the case with the removal of the restriction on legal form of an investment which can now only be a joint-stock company, the application of preferential treatment to both domestic and foreign entities founded even prior to 1 April 1999, the removal of the requirement for a part of domestic natural person, etc.

Even after a possible passage of the aforementioned changes there is much left to be desired. Gaining foreign investment will remain a continual process, for which it should be kept in mind that, alongside environment quality, also environment transparency and predictability, the areas with considerable reserves according to foreign investor views, is one of the determinants.

3.4.4.2. Support for SMEs

Besides support for FDI with the help of which a segment of the restructured industrial capacity can be utilised, support for SMEs is yet another strategic area that constitutes a major opportunity to shift existing capacities toward new areas. Emphasis will be placed on the areas with high added value and the areas with high export share.

On the legislative front, an amendment to Act of the NC SR No. 100/1995 Coll. on state support for SME is needed. The amendment thereto must comply with the European Union’s definition and ensure the required quality growth of institutional provision for SME development. Moreover, the State Aid Act (currently a draft) will be taken into consideration when amending the cited act. This act has been developed in accordance with EU legal requirements and by taking it into consideration when amending Act of the NC SR No. 100/1995 Coll., EU legal requirements will have been reflected therein.

SME medium-term objectives include:

- creation of or making legal, regulatory, administrative and institutional framework more effective to encourage SME investment development and innovation activities,
- support for SME through lowering administrative intensity for businessmen and tradesmen (e.g. by introducing licences or a flat tax for small tradesmen),
- creation of favourable conditions for the entry of domestic and foreign investment into SME (SEED Capital, Joint-Venture, and the like)
- development of and making international co-operation more effective.

In order to accomplish the above objectives, it will be necessary in the area of SME in particular to:

1. reassess the system of granting credit, guarantee and subsidy support programmes with emphasis on enhancing its effectiveness and transparency (fewer programmes with higher concentration of funds and coverage),
2. encourage preferrably transparency and unambiguity of SLE legislation preventing circumvention,
3. set up an intermediary institution between the government and businessmen – A Government Council on SME.

3.5. Activation of the Revitalisation Agency and the Postprivatisation Fund

While specifying its industrial policy, the Ministry of Economy will set specific and measurable (in order for them to become the basis for assessing the performance and rational resource allocation) objectives for administrative bodies of the agencies and fund falling within its province and focused on industrial development.

In the context of industrial policy, the following two institutions, which are expected to be more active, appear most relevant: the Agency for Industrial Development and Revitalisation and the Slovak Postprivatisation Fund.

AIDR (Agency for Industrial Development and Revitalisation)

The AIDR is a Slovak semistate organisation that took up its duties on restructuring in 1996. Its purpose is to bring companies and creditors to a positive approach toward debt reconciliation, debt servicing and corporate restructuring. The AIDR is responsible for the overall implementation of the SPEED programme.

Under the SPEED programme (Slovak programme for companies with excessive indebtedness), the EU Phare programme grants 8 million EUR to the Slovak programme for companies with excessive indebtedness. These funds are available under the 1997 Operative programme for the Slovak Republic (COP 97) which was signed in September 1997 and terminates in 1999. The programme is aimed at improving through providing free consultancy the performance of major production companies where an excessive debt / equity ratio is an acute problem.

The programme is aimed to contribute toward developing of a market economy that would be capable of better withstand pressure from competition in joining the EU. Consultancy provided by the Agency will be implemented particularly in the area of diagnostics; strategy for restructuring; financial, tax, cash and debt management; cost accounting; company appraisal; market and competition analysis; production process assessment including sale of excess assets; investment plans; environmental audits; organisations, human resources and training thereof; contacts and negotiations with foreign investors, etc.

SPEED Phase 1: it expected to complete in 1999. Given a delay in the start of the programme in sifting out appropriate companies meeting the programme entitlement criteria (production company; private ownership; more than 250 employees; a minimum annual turnover of 100 million Sk; not from power engineering, finance, defence production, trade, construction branches, strategic company), it is likely to round out with difficulty (some 30 companies) together with a presentation before the Selection Committee and subsequent approval. There are currently 12 approved companies, 6 more are expected to be approved. In view of the mentioned delay in the start of the programme, granted Phare are expected to be cut by some 2 million EUR.

Phase 2: The AIDR is a programme implementation organisation and is thus responsible for monitoring the programme. Under Phase 2, advisory consortia will start working on in-depth analyses, the preparation of strategic and restructuring plans for companies. This phase is to take about months to complete.

Phase 3: Implementation phase for 10 or so companies for which this phase will be proposed as Phase 2 output.

A plan for extending the restructuring programme – cop ´99

It is obvious from the current experience that it will be necessary to extend assistance not only to those companies which meet the SPEED programme entitlement conditions, but also to those which are currently failing to meet them. The latter include, for example, those companies which will need assistance in geeting prepared for foreign investors. A different situation prevails with those companies which are located in socially sensitive regions with high unemployment.

Keeping in mind the industrial restructuring policy, it would be desirable to launch within the EU Phare a new assistance programme that would address the mentioned problems in the companies not included in the SPEED programme. Basically, this would be an extension of the SPEED programme criteria such that it would encompass also those companies which foreign investors could be interested in and at the same time those which have a significant role in the regions affected. This estimate would bring the number of companies from about 30 under SPEED Phase 2 up to about 60 under the extended programme, and even the number of companies for implementation Phase 3 would rise to about 40. At the same time sectoral studies relating to the use of excess assets and their possible sale would be included here.

The AIDR is expected to be increasingly independent from external support. It is therefore necessary for it to focus more on providing advisory, consultancy and training on a commercial basis, for fees. The foundation of a Centre for Documentation and Information within the AIDR is contemplated. The Centre will store all documents and information on companies and industry through a database in electronic format, which will be definetely valuable not only for foreign investors but also experts on restructuring, regional development, support for export and other programmes. Also contemplated is the issue of specialised publications (journals) on industrial management, including corporate profiles, restructuring activities carried out, special conferences and seminars including advertising.

Slovak Postprivatisation Fund

The Slovak Postprivatisation Fund (hereinafter referred to as ”SPPF”) has been set up in co-operation with the EBRD and the European Union whose operation may be instrumental in restructuring private companies which temporarily have found themselves in a crisis situation. The idea is based on the effect of risk capital in those business entities of the private sector where such resources are not available under the current conditions and criteria for allocation of both domestic and foreign resources. In fact this means that the EBRD and the Foundation for Postprivatisation Business Support as well as the Fund Manager (group of firms Framlington/CET based in London) will invest in them as capital partners, which should imply in addition to a reversal in their liquidity the adoption of new managerial procedures, the opening of new markets, the extension of foreign co-operation and so forth.

The project was approved by virtue of Government Decree No. 354/95 of 23 May 1995 and was scheduled to be implemented from 1 January 1996 onward; it is scheduled to take 10 years to carry through.

The Risk Capital Fund totaling 51.3 million ECU represents a combination of technical assistance (8 million ECU) and equity capital (43.3 million ECU) designed for restructuring and revitalisation of Slovak business entities. From the PHARE programme, 12 million ECU have been earmarked for equity capital and 8 million ECU for technical assistance, while the EBRD is investing 30 million Sk ECU and the Fund Manager 1.2 million ECU.

3.6. Necessary concurrence of other types of state policy

Industrial policy with its content must be intertwined with state economic policy priorities and must influence the ”other” policies; only now can it become a document creating the conditions for growth in competitiveness of industry. From this perspective we must approach the current document as an conceptual and open one to be confronted and brought in line with another documents (Slovakia´s economic policy medium-term priorities, monetary and financial policies and others).

3.6.1. Taxation and public finance

One of the basic and necessary conditions creating the basic framework for Slovak industry development is current efforts to stabilize public finance. Tightening the budgetary discipline is for the benefit of the industrial sphere from the long-term point of view.

An integral part of the above stabilisation efforts must be however measures dealing with the problem of high tax burden for the business sphere. Fundamental action to be necessarily taken in this area includes a marked reduction in the legal entities income tax.

The action should be taken as soon as possible. Indeed, in no other area the state has a tool with which it can accomplish as far-reaching and effective reform in support of the corporate sphere as by means of taxation. By this single measure a far more favourable environment will be created for effective companies and their investment decisions, for job creation in the medium and long term.

A short-term decline in budget revenues will immediately call for changes in heavy budget spending areas (e.g. state administration), but it will be more than offset through increased budget revenues in the medium and long term resulting from a boosted economic activity and rising employment and a subsequent improved tax collection.

Lowering the legal entities income tax rate will at the same time prevent nonproductive tax avoidances, which is currently more than obvious. According to data from Datacentrum for 1997, out of nearly 38,000 companies (joint-stock companies, state-owned enterprises, limited companies and cooperatives) in the Slovak Republic, 20,000 – thus more than a half of the entities – posted a loss. Out of a cumulative loss of 60.8 billion Sk, as much as 96 % (58.2 billion Sk) were concentrated in 5,000 companies and the remaining 15,000 companies posted a loss totaling 2.6 billion Sk, which accounts for a moderate average loss of some 172,000 Sk per company.

It flows from the above data that the first – considerably smaller in number – group of companies is the source of the actually generated loss in the economy, while the basic mass of companies post through ”creative accounting” a moderate loss, which after lowering the tax burden would probably turn into profit with positive effects on the budget revenue side.

Among other taxation measures in support of industrial policy objectives is the clarification of tax legislation and the equalisation of the taxpayer with the tax office.

Changes in the taxation also demand a range of changes in public expenditures, the essence of which is to reduce the degree of redistribution through public finance.

3.6.2. Employment

From the perspective of industrial policy, it is important that employment policy underpin its objectives for a substantial structural transformation of the Slovak economy, which will eventually raise employment and living standards of the population.

For this to happen, certain key reforms in the functioning of the labour market need to be undertaken. This is first of all a more decisive procedure in eliminating the labour discouraging distortions (in the relationship between the minimum wage and earned income, on the one hand, and unemployment or other social benefits, on the other hand.).

Adjustments were partially implemented by virtue of a most recent amendment to the Minimum Wage Act whereby the links between the unemployment benefit and the minimum wage were scrapped.

The need for reducing the employer’s high financial burden is also connected with the reduction of the employer’s transfer burden, which is however conditional on reform of the social security system.

Another key area where progress is needed from the perspective of employees is making more flexible the legislation regulating the rights and obligations of employees and employer in taking in and particularly displacing labour.

The European Union in its study ”Growth, Competitiveness and Employment” notes that complex legislative and administrative procedures (restricting the notice conditions) and the high financial burden (redundancy payment) arising out of the employee protection legislation lower the labour capacity of companies by lowering their operational effectiveness and increase their cost.

This conclusion is borne out also by many international comparative studies, which moreover bring attention to a relatively more adverse impact of the aforementioned legislation on SMEs that have lower capacity to cope with statutory financial requirements.

In the process of harmonisation of labour law with EU law, it will be necessary to incorporate certain institutes such as massive displacement, employer’s information obligations in forming a labour relation, in transfer of a company, given that the present Labour Code fails to meet the criteria of EU directives and regulations.

3.6.3. Competition protection

To provide a competitive environment, it will be necessary to continuously exercise utmost prudence toward high concentrations, create legal instruments for access to large-scale mergers and acquisitions through control over concentrations, and secure a high degree of legal certainty for the business sphere and the speed of strategies for internal market competition.

In this connection, in line with the EU Commission’s requirement for further harmonisation of Slovak competition law with EU law, an amendment to the Competition Protection Act has been developed. The amendment thereto is aimed at transposing the principles of the rule ”de minimis” for agreements curtailing competition, a new wording of the negative certificate institute, introducing a so-called individual exception in the sense of community law, and revoking the current legal state allowing to exempt from the law-mandated prohibition the agreements curtailing competition and the harmonised procedures for businessmen in agricultural production for milk, slaughter animals, oil plants, cereals, sugar beet, vegetables, fruit and potatoes. It is expected to be approved in September and take effect on 1 October 1999 .

Another measure to improve the situation in economic protection is the upcoming law on regulation of natural monopolies to be submitted for discussion of the Slovak Government Legislative Council by the end of 1999.

3.6.4. Infrastructure

As suggested by other countries´ experience, the degree of effectiveness or ineffectiveness of a country’s infrastructure has a substantial impact on the capacity of its business entities to succeed in the fight with international competition.

Therefore it is undeniable that the infrastructure is one of the key factors influencing productivity and competitiveness of Slovak industry and the economy as a whole.

On the other hand, failure to cope with the pace of construction of highways was one of the determinants in destabilizing the environment from whose adverse consequences Slovak industrial companies have suffered to date.

A balance approach toward infrastructure development, which will encompass not only road transport but also rail and water transport as well as energy and telecommunication infrastructures and which will be responsive to the needs of the corporate sphere, on the one hand, and commensurate with the budget financial possibilities, on the other hand, will be critical to their competitiveness in future.

Slovakia needs to make better use of its potential based on a good geographical position. This is true of both river transportation and unutilised possibilities for cargo air transportation, where larger possibilities are emerging for getting Slovak industry involved more intensely in international relations.

From the industry point of view, it is also important that infrastructural branches, including those which have not been thus far exposed to international competition, function in such conditions as will drive them toward transparency, lowering cost, enhancing effectiveness and will not protect a monopoly or dominant position of companies operating in these branches.

3.6.5. Labour education and requalification

The dynamic development of state-of-the-art technologies discussed above and consequent growing demands on the level of labour education and qualifications needed to fully cope with it throw certain doubt on the traditional thesis on highly-skilled Slovak labour.

A decline in economically active population must be offset by growing education of employees. Also the economic advancement determining the utilisation rate of existing education potential should be taken into account in assessing the adequacy of population education levels. From the regional point of view, the distribution of education of the Slovak population is unbalanced – educational centres are in Bratislava, Košice, Nitra, Trenčín, Žilina, Banská Bystrica, Zvolen, Martin and Prešov. The lowest education levels are in south, east and partially north Slovakia where it would be appriopriate to target vocational secondary school development. Non-negligible attention should be devoted even to the development of trade business and related education in trade productions.

Drawing on the comparison between demand from the industrial sphere and supply provided by vocational schools and universities, it should be noted that despite the overall good quality standards of Slovak labour serious shortcomings can be identified just in the most progressive and thus perspective areas.

A lack of labour in highly specialised and expert professions is the result of tardy adaptation of the educational system to new conditions and needs of industries developing more rapidly than the others. Currently, there is demand on the labour market for skilled school-leavers of machine, electrical, textile and garment, construction and chemical industries. Certain industries are facing a grave problem of personnel aging at factories in the labour category - worker.

If flows from the foregoing that the current educational and requalification system should be changed so as to respond more flexibly to the current needs of industry. Both educational instutions and companies themselves must play an active role in this process.

A higher degree of supply – demand harmonisation is of necessity in all the areas:

1. in training the vocational school youth,
2. in requalifying employees or the unemployed,
3. in educating corporate managers,
4. in educating small and medium-sized entrepreneurs.

The most successful are those educational and requalification programmes, in the preparation of which also industrial companies actively participate. Such an approach includes the involvement of companies already in the stage for preparing curricula such that they take account of practical needs of a company, including student vocational training carried out right in the company.

Owing to the shortage of disposable funds Slovak industrial companies insufficiently invest in the education of their employees whose knowledge is thus not upgraded at a reguired pace. Also insufficient is the education of corporate managers.

Unemployment of the young school-leavers is now connected, on the one hand, with the state economic situation and, on the other hand, with the outdated concept of secondary vocational education whose part is also the structure of secondary vocational schools (SVS).. In 1996, a reform of the state administration was effected and all types of secondary school and SVS´s are now administered ex lege by regional offices. A paradox is however that the still effective School Act lays down that the founder of a SVS is that central state administration authority (ministry) to which the appropriate SVS is subject by sectoral orientation. This contradiction or double track management needs to be remedied and stabilized.

3.6.6. Research and development

Slovakia as a small economy cannot set itself the goal to make world-class research and development in all areas, which eventually leads to the application of state-of-the-art technologies. As a result, capacities on this front should be centered around two primary areas:

1. improving competitiveness and quality of existing products,
2. support for such research and development as will help Slovak industrial companies to develop new products which are in demand on the world market.

It is therefore obvious that industrial policy cannot succeed without an integrated and coordinated approach to gaining new modern technologies and their applications in the conditions of Slovak industry, without a close connection between research and the needs for improving industry technological levels and competitiveness.

Less obvious however is how to coordinate these efforts such that means spent on research and development by selected programme directions in industry and the support for innovation development and the National Quality Programme in the business sphere, the purchase of licences and know-how from abroad and in particular the purchase of powerful modern technologies meeting ecological criteria are used as effectively as possible, i.e. stand to gain maximum possible benefits.

In order to render the forms of state R& D support more progressive, enforce transparency in the redistribution of budget resources, engage more actively off-budget resources and augment motivation of the corporate sphere in funding research and development, the following principles are expected to be enforced, in compliance with procedures applied within the EU:

For the benefit of increasing transparency:

- consistently select submitted projects by their intensity into the research category and the development category,
- diversify the amount of support for given categories in compliance with the state support principles applied for R& D from the EU,
- set clear criteria for preferrably supported projects,
- fully apply an integrated approach – work with financial assistance recipents on the part of the state and on a permanent basis,
- create an efficient monitoring and control mechanism for the use of support granted.

For the benefit of increasing effectiveness:

- restrict the volume of nonrepayable – grant – funds in favour of repayable financial supports,
- ensure institutionally their provision under phase 1 through the existing Innovation Fund,
- introduce competition elements into the distribution of funds designated for support for industrial research and open the whole system of another entities,

For the benefit of optimizing the institutional framework:

- improve coordination of activities of relevant institutions responsible for the preparation of material objectives and cofinancing of R& D in industry,
- transform the Innovation Fund into the province of the independent Agency for Support of Research and Development in Industry,
- create personnel and financial prerequisites for the Fund to cope with the demanding role of a turnover fund,
- progressively shift a higher amount of funds into the Innovation Fund.

3.6.7. Environment

Slovak industry cannot afford to snub the worldwide trend toward environmental protection. Indeed, its growing pressure on the restriction or stoppage of those productions that have an adverse impact on the environment.

This trend, which results in the adoption of stringent environmental legislation and regulations and the assuming of obligations arising out of international conventions on environmental protection – as often perceived by industry representatives – only in a threat to the industry development in the form of curtailing environment polluting industrial productions.

This may imply even a development opportunity for industry in case that industry will respond through the development and application of environment-friendly production technologies, procedures and products.

However it will be important at the same time to make sure that environmental protection efforts do not pass into a one-sided campaign against industry as such and against job creation in this area.

3.6.8. Quality and quality system

The National Quality Programme is based on the worldwide knowledge that quality upvalue the market as an utmost and definitive criterion for assessing a product. As a result, quality is becoming a goal, because in order for manufacturers and service providers to be competitive, they must react to the needs and expectations of customers and users.

The principles for applying the quality system are especially desirable for small and medium-sized enterprises. With their application, quality certification is conspicuously coming to the fore on the domestic as well as foreign markets as a categorical requirement. It turns out currently that quality can no longer be perceived only as a technical problem, but also as economic, social and political ones. These requirements are documented in the materials from the Directorate General of the European Commission (DG III-Industry), where main stress is put on:

- strategic business issues,
- sectoral problems (social aspects, employment, regional policy),
- SME development,
- legislation,
- development of human resources and increasing motivation,
- improving apparatus productivity
- development of new technologies and environmental requirements

This means that for placement of our products and services on both the domestic and foreign markets it is necessary to ensure quality, starting from prospectus, production process, after-sale servising, through a complex quality management.

IV. INSTITUTIONAL FRAMEWORK FOR IMPLEMENTING INDUSTRIAL POLICY

4.1. Role of the Slovak Economy Ministry

The key role of the Economy Ministry is: 1. formulate industrial policy, 2. monitor both the internal and external environment in which Slovak industry functions as well as 3. regular industrial policy updating based on new knowledge received through permanent monitoring activity and based on such updating 4. cooperation with relevant branches on necessary changes in legislation.

4.1.1. Formulation of industrial policy

When formulating the objectives and content of an industrial policy, it is necessary to make sure that this role does not only become an internal matter of the Ministry of Economy. Not only the other ministries but first of all external experts should become more involved in its preparation.

To this end, it would be appropriate to restore the activity of the the Industrial Committee to serve as an advisory body to the Economy Minister in the process of industrial policy preparation process.

Experts representing all relevant institutions, including the Slovak Chamber of Commerce and Industry, the Association of Employer's Unions and Associations, Trade Unions, the Academy of Sciences and universities, will be invited to actively work on industrial policy.

4.1.2. Systematic comparison of Slovak industry competitiveness (benchmarking)

A permanent growth in competitiveness of Slovak industry is a necessary and all-important prerequisite for integration of the Slovak economy into the economic zone of EU countries as well as copying with the globalisation effects on our economy.

As already stated above, such a state cannot be achieved through partial arrangements and legal regulations (e.g. by favouring "high-tech" imports, FDI inflows, etc.) and also by implementing industrial policies developed with no relation to economic policy and other partial policies and a required wide professional and information provision.

Permanent growth in competitiveness may only be achieved by abandoning well-established stereotypes in thinking and action (partial solutions) and a shift toward systematic comparison of competitiveness across levels from (supra) national (EU), regional, sectoral to corporate with the status "best at a given level" from among the other countries. Nevertheless, the aim is not just to "map" the instantaneous position, but search for the causes of the status found and in particular search for the methods facilitating such marked an improvement of the position as stand at a given time above the best (benchmarking) level. The aim cannot be merely to permanently approximate and imitate, but in particular an "inspiration with the best" is the case.

Benchmarking is considered even in the EU to be the most important concept of enhancing productivity and competitiveness of European companies as well as competitiveness of the EU economic grouping on the globalizing markets.

The EU strategy for benchmarking is of importance to the Slovak Republic not only because this is one of major strategies to apply in EU countries on industrial policy, but especially because it constitutes for such economy in transit as Slovakia a ”strategy for faster progress” – not through imitation or emulation but rather as an inspiration to mobilize internal reserves with the use of international cooperation too.

The Slovak Economy Ministry will therefore initiate – again in close cooperation with other economic branches, the Agency for Support of SME, the Association of Employer's Unions and Associations (AZZZ), the Chamber of Commerce and Industry, the School of Economics and the Slovak Academy of Sciences – foundation of the ”Slovak Benchmarking Information Centre” (SBIC) whose activity should become a significant part of the state industrial policy.

4.1.3. Providing Slovakia's active participation in EU initiatives on industrial policy

In connection with Slovakia's aspirations for EU membership, it will be important for the country to take active part in the initiatives declared on industrial policy by the European Commission (DG III and DG IA):

1. The Industrial Forum on Enlargement to exchange information on industrial aspects of the preaccession strategy,
2. The Programme for Business Support focused on assistance to business associations from the applicant CCE countries,
3. TAIEX (Technical Assistance Information Exchange Office) seminars on various aspects of the preaccession strategy to be held on request from an applicant country,
4. dialogue between EU industries and candidate countries e.g. through meetings of industry directors general.

4.2. Concurrence of the other sectors

Competitiveness of Slovak industry will be even in the medium term conditional on the state's capacity to favourably influence developments of such environment parameters as tax and transfer burden, labour market flexibility, law enforcement, transparency, etc.

Without close concurrence – and in particular coordination of approaches – of the Economy Ministry responsible for industrial policy, on the one hand, and respective departments responsible for setting the aforementioned environment paramaters, on the other hand, an improvement of the performance of Slovak industry business entities and a marked improvement of their competitiveness in the world market is not thinkable.

A more complex approach to industrial policy thus envisages the overcoming of a – often prevailing – narrowly department view and requires a harmonisation of respective ministries whose measures have a significant impact on industrial policy.

IV. CONCLUSION

Following the 10 years of transformation it should be noted that Slovak industry and the whole economy face the need for a sweeping and deep-seated restructuring. The hitherto industrial policy has failed.

Both the overall hitherto economic policy and hitherto industrial policy: 1. not only could not create conditions for a reversal in the Slovak industry structure, but in particular 2. have shown that other approach is needed to improve the performance of industrial companies, an entirely new definition of the content, principles, objectives, instruments and institutional framework for industrial policy is needed.

Over the previous period, the basic reason for the failure of the state policy was wrong prioritizing. The state with its policy (expansionary budget policy, nontransparent privatisation) destabilised the environment and then attempted to deal with unfavourable results through inadequate interventions in the microsphere (Revitalisation Act).

Based on the needs of Slovak industry and the whole Slovak economy, industrial policy faces a task of adopting a range of measures through the implementation of which the following is to be accomplished:

· reduction in redundant capacities of Slovak industry in those areas which are not competitiveness and which long termly tie down substantial production capacities and labour, thereby conserving the existing – thus inconvenient – industrial structure. The release of such capacities – while considering the impacts of requisite restructuring on unemployment and regions – that are currently concentrated in traditional industries, is a step necessary to shift economic activities toward more modern industries.

· parallely shifting production factors (capital, labour, technologies) toward new areas which should take account of the global context, trends in crucial factors influencing future developments of the competition environment within which Slovak industry will be operating in the decades to come.

· enhancing competitiveness of Slovak industry, which can only occur provided that the two aforementioned processes have been successfully implemented and which is a sine qua non for success of Slovak industry in the world’s markets.

Expectations of the public, which it formulates in relation to the whole Slovak economy and which most often include the following, cannot be deemed to be realistic until the above objectives for Slovak industry have been accomplished.:

1. a marked reduction in unemployment,
2. improving living standards,
3. improving the quality of life.

The basic prerequisite for success of the new industrial policy is the focus of primary attention on systematic creation of a favourable environment for business, which however cannot be provided with just a narrowly perceived, traditional industrial policy, but all of the other relevant state policies and industries responsible for their implementation must get involved in its creation.

The establishment of an effective institutional framework for implementing industrial policy will require to: 1. formulate an industrial policy, 2. monitor both the internal and external environment in which Slovak industry functions as well as 3. regular industrial policy updating based on new knowledge obtained through permanent monitoring activity.

The key role in industrial policy will continue to be played by the Ministry of Economy that will:

1. set up a Council for Industrial Policy as an advisory body for the Economy Minister on industrial policy formulation
2. establish a ”Slovak Benchmarking Information Centre” (SBIC) and will adapt accordingly the job descriptions for responsible employees with a view to benchmarking Slovak industry competitiveness
3. coordinate work on creating the conditions for considerably increasing risk, development and strategic capital inflows into the Slovak corporate sphere
4. prepare a proposal for establishing an information system on financial performance and quality of assets and liabilities for restructured companies
5. coordinate the Slovak Republic’s active participation in EU initiatives declared on industrial policy by the European Commission (DG III and DG IA).